



2004 Montana Net Operating Loss Instructions Montana Form NOL

15-30-117, MCA and 42.15.116, ARM

Introduction

If your deductions for the year are more than your income for the year, you may have a net operating loss (NOL). An NOL year is the year in which an NOL occurs. You can use an NOL by deducting it from your income in another year or years.

To have an NOL, your loss must generally be caused by deductions from your:

- trade or business,
- work as an employee,
- casualty and theft losses,
- moving expenses, or
- rental property.

A loss from operating a business is the most common reason for an NOL.

Part-Year Resident, Nonresident and Composite Tax Return Participants

A Montana NOL cannot be created when the Montana source income (loss) reported on Montana Form 2A, Schedule III is a loss. In calculating a NOL for a part-year resident or a nonresident you must include, in your calculation both Montana and non-Montana source income which is included on the Montana Form 2, line 40.

A partnership or S. corporation who files a composite income tax return on behalf of its partners or shareholders cannot create a Montana NOL by reason of a partnership or S. corporation reporting a Montana loss on the composite return. For a participating partner or shareholder to generate a Montana NOL, the partner or shareholder must file separately a Montana Form 2 reporting his or her total Montana and non-Montana source income.

How to Figure an NOL

There are rules that limit what you can deduct when figuring an NOL. In general, the following items are not allowed when figuring an NOL.

- Any deduction for personal exemptions
- Capital losses in excess of capital gains
- The section 1202 exclusion of 50% of the gain from the sale or exchange of qualified small business stock

- Nonbusiness deductions in excess of nonbusiness income
- NOL deduction

When computing the NOL, carrybacks, carryovers, and refund limits of taxpayers whose marital or filing status has changed, the federal rules and instructions applicable to change in marital status and change in filing status apply.

A nonresident who owns a business that operates both in and outside of Montana must follow the division-of-income provisions of the Multistate Tax Compact and the principles of allocation and apportionment to determine the amount of the business-wide loss attributable to Montana.

Schedule A

Use Schedule A, Form NOL to figure your NOL.

Line 1. Enter the amount from your 2004 Montana Form 2, line 40. If line 1 is a negative amount, you may have an NOL.

Line 6 – Nonbusiness deductions. Enter on line 6 deductions that are not connected to your trade or business or your employment. Examples of deductions not related to your trade or business are:

- alimony,
- contributions to an IRA or other self-employed retirement plan,
- itemized deductions (except for casualty and theft losses and any employee business expenses), and
- the standard deduction (if you do not itemize your deductions).

Do not enter business deductions on line 6. These are deductions that are connected to your trade or business. They include the following.

- Federal income tax paid on business profits
- Moving expenses
- The deduction of one-half of your self-employment tax or your deduction for self-employed health insurance
- Rental losses
- Loss on the sale or exchange of business real estate or depreciable property

- Your share of a business loss from a partnership or S. corporation.
- Ordinary loss on the sale or exchange of stock in a small business corporation or a small business investment company.
- If you itemize your deductions, casualty and theft losses (even if they involve nonbusiness property) and employee business expenses (such as union dues, uniforms, tools, education expenses, and travel and transportation expenses).
- Loss on the sale of an accounts receivable (if you use an accrual method of accounting).
- Interest and litigation expenses on state and federal income taxes related to your business.
- Unrecovered investment in a pension or annuity claimed on a decedent's final return.

To determine the portion of a deductible expense attributable to income from a trade or business, the expense must be multiplied by the ratio of net income from the trade or business to Montana adjusted gross income.

When calculating the portion of federal tax attributable to trade or business income, the ratio must be calculated using the net business income and Montana adjusted gross income for the year the federal tax was incurred.

Line 7 – Nonbusiness Income. Enter on line 7 only income that is not related to your trade or business or your employment. For example, enter your annuity income, dividends, and interest on investments. Also, include your share of nonbusiness income from partnerships and S. corporations.

Do not include on line 7 the income you received from your trade or business or your employment. This includes salaries and wages, self-employment income, and your share of business income from partnerships and S. corporations. Also, do not include rental income or ordinary gain from the sale or other disposition of business real estate or depreciable business property.

Line 17 – Adjustment for Section 1202 Exclusion. Enter on line 17 any gain you excluded under section 1202 on the sale or exchange of qualified small business stock.

Lines 19- 22 – Adjustments for Capital Losses. The amount deductible for capital losses is limited based on whether the losses are business capital losses or nonbusiness capital losses.

Nonbusiness capital losses. You can deduct your nonbusiness capital losses (line 2) only up to the amount of your nonbusiness capital gains without regard to any section 1202 exclusion (line 3). If your nonbusiness capital losses are more than your nonbusiness capital gains without regard to any section 1202 exclusion, you cannot deduct the excess.

Business capital losses. You can deduct your business capital losses (line 11) only up to the total of:

- Your nonbusiness capital gains that are more than the total of your nonbusiness capital losses and excess nonbusiness deductions (line 10), and
- Your total business capital gains without regard to any section 1202 exclusion (line 12).

Line 23 – NOLs from other years. You cannot deduct any NOL carryovers or carrybacks from other years. Enter the total amount of your NOL deduction for losses from other years.

When to Use an NOL

Generally, if you have an NOL for a tax year ending in 2004, you must carry back the entire amount of the NOL to the two tax years before the NOL year (the carryback period), and then carry forward any remaining NOL for up to 20 years after the NOL year (the carryforward period). You can, however, choose not to carry back an NOL and only carry it forward. You cannot deduct any part of the NOL remaining after the 20-year carryforward period.

NOL year. This is the year in which the NOL occurred.

Exceptions to Two-Year Carryback Rule

Eligible losses and farming losses qualify for longer carryback periods.

Eligible loss. The carryback period for eligible losses is three years. An eligible loss is any part of an NOL that:

- is from a casualty or theft, or
- is attributable to a Presidentially declared disaster for a qualified small business.

Qualified small business. A qualified small business is a sole proprietorship or a partnership that has average annual gross receipts (reduced

by returns and allowances) of \$5 million or less during the three-year period ending with the tax year of the NOL. If the business did not exist for this entire three-year period, use the period the business was in existence.

Farm loss. The carryback period for a farming loss is five years. A farming loss is the smaller of:

- The amount which would be the NOL for the tax year if only income and deductions attributable to farming businesses were taken into account, or
- The NOL for the tax year.

Farming business. A farming business is a trade or business involving cultivation of land, raising or harvesting or any agricultural or horticultural commodity, operating a nursery or sod farm, raising or harvesting a tree bearing fruit, nuts, or other crops, or ornamental trees. The raising, shearing, feeding, caring for, training and management of animals is also considered a farming business.

A farming business does not include contact harvesting or an agricultural or horticultural commodity grown or raised by someone else. It also does not include a business in which you merely buy or sell plants or animals grown or raised by someone else.

Waiving the Five-year Carryback

You can choose to treat a farming loss as if it were not a farming loss. If you make this choice, the carryback period will be two years. To make this choice, indicate the carryback years in the box provided for on Schedule A before the due date (including extensions) that you are choosing to treat a 2004 farming loss as if it were not a farming loss. Once you waive the five-year carryback, it is irrevocable.

If you choose not to carry back any of your farming loss, check the appropriate box on Schedule A which states that you are electing to forgo the carryback and carry forward your farming loss.

Waiving the Carryback Period

You can choose not to carry back your NOL. If you make this choice, then you can use your NOL only in the 20-year carryforward period.

To make this choice, check the box on Schedule A, electing to forgo the carryback of your NOL. This election must be made by the due date (including extension of time) for filing the tax

return for the tax year of the NOL. Once you elect to waive the carryback period, it is irrevocable. If you choose to waive the carryback period for more than one NOL, you must make a separate election for each NOL year.

Schedule B

Complete and file this schedule to determine the NOL deduction for each carryback year and the amount to be carried forward, if not fully absorbed.

If an NOL is more than the Montana modified taxable income for the earliest year to which it is carried, you must file Schedule B to figure the amount of the NOL to be carried to the next tax year. The amount of the carryover is the excess, if any, of the NOL carryback over the modified taxable income for that earlier year. Montana modified taxable income is the amount figured on line 8 of Form NOL, Schedule B.

If you carry two or more NOLs to a tax year, figure your modified taxable income by deducting the NOLs in the order in which they were incurred.

Line 1 – Enter the amount shown on Form NOL, Schedule A to the appropriate carryback year. See “When to Use an NOL” discussion above to determine your carryback year. If an NOL is not fully absorbed in a year in which it is carried, complete Schedule B to figure the amount of the NOL carryover to the next year.

Line 2 – Do not take into account on this line any NOL carryback from 2004 or later. However, do take into account NOLs that occurred in tax years before 2004 and are otherwise allowable as carrybacks or carryovers.

Line 3 – Net Capital Loss Deduction.

Individuals. Enter as a positive number the amount, if any, shown (or as previously adjusted) on Schedule D (Form 1040). If married filing separate returns for Montana, include the capital loss limitation adjustment in calculating Montana adjusted gross income.

Estates and trust. Enter as a positive number the amount, if any, shown (or as previously adjusted) on Schedule D (Form 1041).

Line 4 – Section 1202 Exclusion. Enter as a positive number any gain excluded under section 1202 on the sale or exchange of qualified small business stock.

Line 5 – Adjustments to Montana Adjusted Gross Income. If you entered an amount on line

3 or line 4, you must refigure certain income and deductions based on Montana adjusted gross income. These include:

- the special allowance for passive activity losses from rental real estate activities,
- Montana taxable social security benefits,
- IRA deductions,
- excludable savings bond interest,
- student loan interest deduction, and
- tuition and fees deduction.

For purposes of figuring the adjustment to each of these items, your Montana adjusted gross income is increased by the total of the amounts on line 3 and line 4. Do not take into account any NOL carryback from 2004 or later.

Line 6 – Adjustment to Itemized Deductions.

Individuals. Skip this line if, for the applicable carryback year:

- you did not itemize deductions, or
- the amounts on Schedule B, line 3 and line 4, are zero.

Otherwise, complete lines 10 through 34 and enter on line 6 the amount from line 34 (or, if applicable, line 12 of the itemized deduction worksheet on Form NOL, page 2).

Line 9 - NOL Carryover. After completing all applicable columns, carry forward to 2005 the amount, if any, on line 9 of the column for the first preceding tax year.

Line 22 – Refigured Charitable Contributions. Refigure your charitable contributions using line 20 as your adjusted gross income unless, for any preceding tax year:

- You entered an amount other than zero on line 19, and
- You had any items of income or deductions based on adjusted gross income that are listed in the instructions for line 5 of Schedule B above.

Schedule C

Use Schedule C, Form NOL to summarize your NOL absorption.

NOL Generated. Enter the amount of the NOL generated as reported on Schedule A, line 24.

NOL Absorbed. Enter the amount of the NOL absorbed as reported on Schedule B, line 8.

NOL Balance. Remaining balance of NOL to be applied to next carryover period.